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SENSITIVE

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SUBJECT: AMBASSADOR DISCUSSES ECONOMIC AGENDA WITH FINANCE MINISTER

**¶1.** (SBU) Summary and Introduction. In a private February 1 meeting with Finance Minister Palocci, Ambassador emphasized the need for the GOB to continue making progress on its micro-economic reform agenda. Discussion, in particular, focussed on the GOB's recently-enacted Public-Private Partnership regime and how the GOB might best attract U.S. investors. Ambassador emphasized the importance of strengthening the country's investment climate by streamlining bureaucracy, increasing transparency, and establishing clearer rules of the road. On specific issues, Ambassador queried Palocci about the status of the GOB's ratification of the Capetown convention, Brazilian intentions regarding debt-for-nature swaps, and prospects for facilitating express delivery operations in Brazil as well as lowering GOB tariffs on such services. Palocci made clear that the USG should feel free to bring to him issues of concern (whether economic in nature or of broader import) and that he could ensure that these matters reached the President's attention. End Summary and Introduction.

**¶2.** (SBU) The Ambassador's February 1 meeting with FinMin Palocci, scheduled at post's initiative, took place just after the Minister's return from the World Economic Forum in Davos and just prior to his departure for London for a BRIC/G-7 breakfast. (The meeting was a one-on-one affair, in accordance with Palocci's specific request.) As in Davos the GOB delegation (consisting of President Lula, Chief of Staff Dirceu, Central Bank Chief Meirelles, Trade Minister Furlan as well as Palocci) focused on wooing investors to Brazil, during the session with the Ambassador increasing FDI in Brazil was uppermost in the FinMin's mind.

**¶3.** (SBU) Palocci stated that with the enactment of the Public-Private Partnership legislation in late December 2004, now was the time for U.S. investors, particularly those specializing in transportation infrastructure, to consider Brazil. The Ambassador responded that with the recent passage of new bankruptcy legislation, judicial reform, and an innovation law, Brazil was indeed moving forward on its micro-reform agenda. However, he added, the country could do even more to improve the investment climate, i.e., by streamlining its cumbersome regulatory bureaucracy, promoting greater transparency, and establishing clearer rules of the road.

**¶4.** (SBU) Palocci took these points, noting that the GOB indeed realized that its reform agenda had not been completed and that it had to continue to hold the line in terms of fiscal discipline. He presented the Ambassador with a copy of a detailed Ministry study setting forth the GOB's plans for future taxation, pension, and regulatory reforms. With respect to the fiscal side, Palocci declared that notwithstanding pressure from those who wanted to increase government spending, the GOB planned to maintain a healthy primary surplus in 2005.

**¶5.** (SBU) Ambassador then raised a series of issues involving the U.S.-GOB bilateral economic/commercial relationship.

-- Capetown Convention. Ambassador urged Brazil to consider joining the Capetown Convention, which establishes, among other things, rules that facilitate the seizure of aircraft that have been put up as collateral on loans that go into default. Support for the Convention was strong in both countries, he said, with Ex-Im Bank pushing for it in the U.S. and Brazilian aircraft maker Embraer in Brazil. Palocci promised to look into the matter, which, it appears, is currently being considered by an interagency Brazilian committee.

-- Debt-for-Nature Swaps. Noting that such swaps are possible under the Tropical Forest Conservation Act, Ambassador queried Palocci as to what Brazil's intentions were on this issue. The FinMin was enthusiastic about the

idea, replying that he would speak with Lula about it. Another follow-up item which he would pursue, he continued, would be to invite the Governor of Acre state (part of the Brazilian Amazon) to Brasilia for a discussion with the Ambassador and himself. Note: Contemporaneous contacts with working-level Ministry officials revealed that prior to submitting a debt-for-nature swap proposal to Treasury, the GOB needs to shore up its legal framework. Ministry staffers are currently drafting the necessary regulations on an urgent basis.

-- Tax Treaty. Ambassador inquired what was the GOB's thinking regarding a bilateral tax treaty. Palocci responded that the GOB wanted to move forward on this and that he felt that discussions were currently in the "right channels." Note: this was probably a reference to the Treasury-led Group for Growth, which last met in December 2004.

-- Express Delivery Services. Noting that that post had written Palocci in December 2004 requesting that the GOB lift restrictions on express delivery operations and lower GOB tariffs on such services, Ambassador queried where the GOB was on this issue. Palocci responded that he would look into the matter, and get back to the Ambassador in a timely fashion.

-- Digital Television. Ambassador advocated for GOB adoption of the U.S. ATSC digital television standard. (Although not specifically under the purview of the FinMin, Ministry reps sit on the interagency committee that is reviewing the standard issue; during late 2004 Ambassador had advocated in favor of ATSC with Minister of Communications Oliveira). FinMin Palocci took note of our concerns.

16. (SBU) In closing, Palocci made clear that the Ambassador should feel free to bring to him matters of concern to the USG, whether such issues were economic/commercial in nature or not. The FinMin declared that he would make certain that the items that the USG felt were important got to the President's attention.

DANILOVICH